

EXECUTIVE SECRETARIAT
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Executive Secretary
9/20/83
Date

THE SECRETARY OF THE TREASURY
WASHINGTON 20220

July 27, 1983

MEMORANDUM FOR THE VICE PRESIDENT
THE SECRETARY OF STATE
THE SECRETARY OF DEFENSE
THE SECRETARY OF AGRICULTURE
THE SECRETARY OF COMMERCE
THE DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET
DIRECTOR OF CENTRAL INTELLIGENCE
UNITED STATES TRADE REPRESENTATIVE
ASSISTANT TO THE PRESIDENT FOR
NATIONAL SECURITY AFFAIRS
ASSISTANT TO THE PRESIDENT FOR POLICY DEVELOPMENT
CHAIRMAN, COUNCIL OF ECONOMIC ADVISORS

SUBJECT IG-IEP Study of Proposed Barter Arrangements

Recently several proposals have been made concerning barter arrangements involving CCC commodities and strategic materials. They have included:

- Bills introduced in Congress to broaden CCC authority to enter into barter arrangements with our foreign trading partners;
- Agency proposals to dispose of specific CCC commodities or to acquire specific strategic materials through barter;
- Foreign government proposals for bartering strategic materials for CCC commodities; and
- Private sector proposals to assist agricultural exports through barter for strategic materials.

These proposals raise several policy issues which need to be addressed, such as those affecting: (1) trade policy; (2) CCC disposal policy; and (3) strategic stockpile acquisition and funding policies.

I have asked Marc Leland to chair a meeting of the IG-IEP to review these arrangements with the intent of developing a decision memorandum for SIG-IEP consideration. He will be in contact with representatives of your agencies shortly to arrange the meeting.



Donald T. Regan

Pending Barter Legislation and Scheduled Hearings

<u>Bill and sponsor</u>	<u>Title</u>	<u>Precis</u>
H.R. 1677 Wortley (R.-NY)	The Agricultural Export Equity Act of 1983	Funds from the CCC will be used for export assistance for U.S. agricultural commodities.
H.R. 2428 Evans (R.-Iowa)	Amends CCC Act.	Amends CCC Act to promote the exchange of materials produced abroad and needed in the U.S. for agricul- tural commodities produced in the U.S. through normal commercial channels.
H.R. 3295 Evans (R.-Iowa)	Amends CCC Act.	Amends CCC Act to promote the exchange of surplus dairy stocks for other materials. Encourages barter by allowing private sector proposals to use CCC stocks.
H.R. 3544 Bennett (D.-Fla)	Amends the Stock Piling Act	Amends the Stock Piling Act to provide for surplus materials from Government agencies to be included in the stockpile, sets up barter commission and makes the transaction fund a revolving fund.
S. 822 Helms (R.-N.C.)	To expand markets for U.S. agricul- tural commodities	Expands the authority for the use abroad of CCC stocks, requires the sale of CCC dairy products and improves programs under P.L. 480. Amends CCC Act to require bilateral arrangements.
S. 1683 Humphrey, Symms Nickles	A bill to facilitate the efficient use of barter in managing stocks in CCC and national defense.	Allows multilateral barter, mandates use of U.S. trad- ing firms and removes requirement that CCC be reimbursed.

S. 251 Helms (R.-N.C.)	Agricultural Export Equity Act of 1983	Amends CCC Act to require export sale of CCC dairy stocks and provides for barter of such stocks.
S. 1703 Jepsen	Exchange excess of CCC dairy stocks for materials for the strategic stockpile.	Encourages barter by allow- ing private sector to use CCC stocks.

Scheduled Hearings

<u>Topic</u>	<u>Committee</u>	<u>Date</u>
Stockpile (will include barter)	House Armed Services (Bennett (D.-Fla.))	To be announced
Stockpile (will include barter)	Senate subcommittee on Preparedness (Humphrey R.N.H.)	September

BACKGROUND

U.S. Barter Experience

Throughout its history barter was seen as a tool to accomplish other policy objectives, and not as a primary tool to enhance overall benefits from trade. For instance, in the first decade of barter the intention was to export surplus agricultural commodities in order to avoid depressing U.S. markets. The legislative history suggests Congress intended to provide a policy guideline of encouraging exchanges of these surpluses for strategic materials, and to take advantage of spot opportunities to dispose of our agricultural glut and at the same time to fill the stockpile.

However, successful barterers using either surplus CCC stocks or materials excess to the strategic stockpile to acquire needed materials for the latter are dependent on finding countries needing our excesses and which can supply commodities needed for our strategic stockpile. In other words, there must be a double coincidence of wants. Such difficulties mean compromises must be reached: we end up with materials for the stockpile which are less than high priority although we are short of them, while the supplying country may have to accept commodities which satisfy secondary needs. An illustration is the several recent barterers of CCC stocks for Jamaican bauxite. While the Jamaicans would have preferred grains they had to be satisfied with NFDM, while we had to accept bauxite which, although in deficit is a lower priority compared to other deficits in the strategic stockpile. Jamaica's foreign exchange difficulties, its excess capacity in bauxite and the Administration's desire to demonstrate effective support for the Seaga government combined to outweigh pure stockpile considerations. Thus, in many, although not all, barter transactions, it is the expediency of other needs and policies for which the barter provisions of legislation governing the CCC and the strategic stockpile happen to fit and can be moulded to achieve those goals.

A variety of barter mechanisms have been authorized, most of which were used 20 years ago or more, including bilateral and multilateral barterers. The importance of each has changed over time and, depending on the mechanism used, can impact dramatically on such issues as USG treaty obligations, foreign relations, and market developments. Existing CCC law authorizes only bilateral barter agreements which do not displace cash sales. If private traders are used to complete the transaction, CCC can lose control over the final imputed prices, thus opening up the possibility of abuse of trading rules and put us in potential violation of GATT rules or in conflict with other foreign or domestic producers of the affected commodities. Also, use of private firms cannot guarantee that such barter does not replace cash sales, as is mandated by governing legislation.

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CCC barterers generally contain elements of export subsidies to the recipients. In the early years, the amount of the subsidy was not subject to CCC controls because third party commercial intermediaries negotiated substantially more value for the materials than they paid CCC. In the recent contracts, there is an element of subsidy since CCC has received much less than acquisition value (in terms of the acquired bauxite) for its bartered agricultural commodities.

Assessment of the impact on trade policy of past barterers involving CCC commodities and stockpile materials has been virtually nil. In the several studies and reviews which have been made since the early sixties, only one devoted space to the issue of trade policy impact. In only three sentences it asserted there was a conflict between bilateral barter and U.S. trade policy -- no analysis was made. There have been only a few references to our obligations under international treaties such as GATT and how barter interacts with them. Currently, however, there is an interagency group studying U.S. countertrade policy including barter.

All the statutes governing barter contain in one way or another the following dictum: barter or exchange should be considered where it serves the national interest in terms of domestic or foreign policy goals. The interpretation of 'national interest' is subject to wide variation. In some periods, it meant using barter to dispose of excess CCC commodities even at the risk of subsidized prices. During the 1960's targets for materials in the stockpile changed often, resulting in fluctuating use of barter and cash sales to adjust the composition of the stockpiles. The use of CCC-stockpile barterers was phased out during the late 1960's and early 1970's as the surpluses of CCC commodities were eliminated and stockpile goals were cut back.

Although much has been written on the subject of barter, there has been little analysis to date regarding its implications under the GATT. This has been in large part due to the fact that countertrade including barter was not envisaged as a problem at the time of Articles of the GATT were drawn up in the 1940's. Although the consequences of barter could be similar to the consequences of other practices which are GATT-illegal, barter itself has not been found to be illegal under the GATT. Most trade experts would say, however, that it violates the spirit of the open, market-determined, multilateral trading system sought by GATT. An ongoing interagency review of countertrade has concluded, after a review of the GATT Articles, that countertrade, if imposed by governments, runs counter to a number of fundamental GATT rules.

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Barter goods imported into the United States are subject to U.S. trade laws. The statutes providing for import relief from injurious or disruptive imports (Sections 201 and 406 of the Trade Act of 1974) can be applied to the bartered goods on the same basis as goods imported under normal commercial transactions. However, barter introduces a lack of transparency which can make it possible for a government to subsidize -- including our own government when engaged in bilateral barters such as those involving CCC and stockpile commodities -- or dump exports when such actions would not be possible through normal channels. This lack of transparency opens up the realm of abuses of trading rules by governments, including our own, thereby putting us in probable violation of GATT regulations. Antidumping and countervailing duty statutes and their applicability to countertraded goods raise a number of legal questions, which must be answered before stockpile barters and exchanges are allowed to continue.

Strategic Stockpile Organization and Policy Mechanisms

The strategic stockpile consists of almost 100 "strategic and critical" materials. It is over 30 years old. Due to changing estimates of wartime industrial needs (determined quadriennially by FEMA on the hypothesis of a 3-year conventional war), many holdings are excess to current stockpile goals, while others are deficient compared to new goals. Goals with excess commodities are valued at \$5 billion while those in deficit are valued at \$10 billion. PL 96-41, passed in 1979, revised basic stockpile policy law by creating a stockpile transaction fund which would receive the proceeds of sales of surplus inventories and serve as a pool of funds for buying commodities in deficit. The fund is not a revolving fund, and both disposals and acquisitions need authorizing legislation, while acquisition monies have to be appropriated from the fund. In addition to outright cash sales, the Stock Piling Act permits -- does not mandate -- the use of barter as a tool by which the GSA can dispose of excess materials and reduce the deficit materials. The GSA can use its own excess materials to exchange them directly for materials which are below goal.

Policy planning and operation of the strategic stockpile is accomplished through an interagency process authorized by PL 96-41, the Stock Piling Act, and by Executive Order 12555. Through the Executive Order, the President delegated the policy planning function to the Federal Emergency Management Agency (FEMA) and the operational functions to the General Services Administration (GSA). The policy planning and operational functions are formulated annually in the Annual Materials Plan (AMP), which is prepared by the Annual Materials Plan Steering Committee (AMPSC) an interagency staff group. The AMPSC is composed of two permanent subcommittees: Strategic Implications; and Market

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and International Political Impacts. In mid-1982, an ad hoc subcommittee on barter was formed. Attachment A outlines the organizational structure and member agencies.

Attachment B briefly describes the Annual Materials Plan process. Each year this process produces a list of acquisitions and disposal actions for stockpile materials. The process is initiated by FEMA, which provides to GSA a list of goals, shortfalls, excesses and the priorities for each material according to its importance to a wartime effort. After an evaluation of the market outlook, GSA proposes quantities of commodities for acquisition or disposal during the current year. These proposals are provided to the two permanent AMP subcommittees for their review. Differences between subcommittee and GSA recommendations are then resolved by the Steering Committee and submitted to the Director of FEMA for approval.

The agreed upon AMP is submitted by FEMA to the National Security Council (NSC) for its review and a copy is given to OMB for information. Any further revisions are made jointly by these three agencies. The final AMP is transmitted to the House and Senate Armed Services Committees for approval and appropriations for acquisitions.

Until early 1982, all acquisitions and disposals were made for cash. Beginning then, and as a result of Jamaica's interests in selling and bartering its bauxite to the stockpile and the existence of excess CCC dairy stocks, bartering has received increasing attention. The ad hoc subcommittee on barter of the AMPSC was established to develop lists of available CCC commodities and countries which could use these commodities in exchange for materials they could provide for the stockpile. Since last year, the subcommittee has become moribund, and barter activities of this sort have come under the direct aegis of USDA and NSC.

At first the CCC staff opposed bartering its stocks mostly because it would have to accept a GSA IOU payable several years hence. Now, they have come to accept the concept as a means of reducing burdensome and costly stocks of agricultural commodities, and USDA has urged, for example, a barter of Mexican flourspar for CCC dairy commodities. The USDA analysis of this particular opportunity showed little recognition of impacts on trade policy, treaties and relations with other nations.

This brief review shows there is no definitive, formal policy on bartering of excess CCC stocks for stockpile materials. It is a temporary coincidence that USDA and GSA are able to arrange a few barters at this time as each seeks its own objectives.

The only recent instance of a coordination of stockpile policy or operations with trade policy through the TPC mechanism was the recent FEMA request to seek a waiver from open solicitation (both

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foreign and domestic bidders) for the strategic stockpile acquisition of titanium, and to limit such acquisition to domestic suppliers. The TPC became involved because the 1979 Trade Agreements Act effectively prohibits Buy American features from commodities (and finished goods) under the jurisdiction of STR. In practice, all commodities in the strategic stockpile are under the Act's regulations and STR jurisdiction. While the titanium review was comprehensive, it addressed only this single case, and did not focus on overall policy issues and inter-relationships among affected policies.

Under Section 6 of the Stock Piling Act of 1979, disposals are to be made to domestic users to the maximum feasible extent. Any deviation from this, as in the case of tin, is generally reported to the Congress as a matter of courtesy, but not clearance. This aspect of stockpile management has not been scrutinized in terms of impacts on other policy issues such as trade, treaties and relations with other nations.

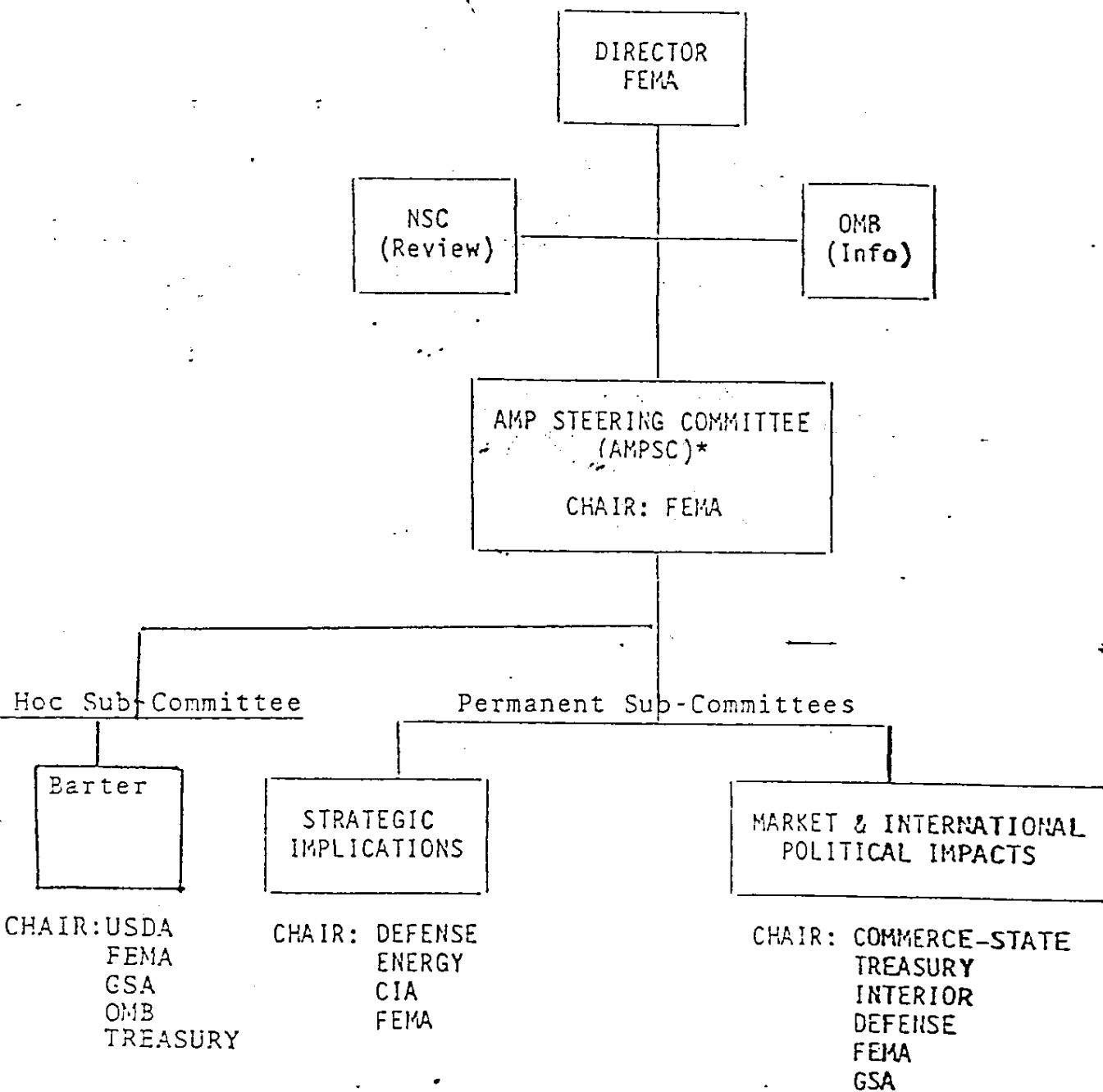
Finally, an interagency review is underway of the economic assumptions and procedures underlying the national defense stockpile goals. This examination is being done at the behest of CCEA which is in response to OMB's sharp criticism of FEMA's methods and assumptions in determining the stockpile goals. Pursuant to the review, it is expected that the economic agencies -- CEA, Treasury, and OMB will play a larger role in determining goals and overseeing stockpile management. The goals are scheduled for review this year, but completion of the process will be delayed until next year if necessary to take advantage of the interagency policy review.

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ANNUAL MATERIALS PLAN (AMP) STRUCTURE



* AMPSC MEMBERS:

FEDERAL EMERGENCY MANAGEMENT AGENCY (FEMA)
DEPARTMENT OF THE INTERIOR
DEPARTMENT OF THE TREASURY
CENTRAL INTELLIGENCE AGENCY (CIA)
GENERAL SERVICES ADMINISTRATION (GSA)
OFFICE OF MANAGEMENT & BUDGET (OMB)

DEPARTMENT OF STATE
DEPARTMENT OF ENERGY
DEPARTMENT OF DEFENSE
DEPARTMENT OF COMMERCE
DEPARTMENT OF AGRICULTURE
NATIONAL SECURITY COUNCIL (NSC)

THE ANNUAL MATERIALS PLAN PROCESS

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Source and Input

Agency Review

Goal Setting
and
Annual Acquisitions,
Disposals

ational
Security
Council

(Presidentially-Approved
(Policy Guidance
((Scenario, Priorities)

Commerce

(Consumption Patterns
(Industrial Capacity
(Agricultural Commodities
(by Countries
(Agricultural Substitution

Defense

(Military Requirements
(
(Transportation Losses

Interior

(Supply: Non-Agricultural
(Commodities by Country
(Non-Agricultural
(Substitution

State

(Political and Economic
(Factors for Foreign
(Countries

----->

Unique Defense
Requirements
(Defense, Energy)

Other Strategic
Implications
(Defense, CIA, FEMA, Energy)

Market and International
Economic and Political
Impacts
(Commerce, State, FEMA, GSA,
Treasury, Interior, Defense)

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FEMA

Determine
Goal
By
Commodity

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NSC

Review

ATTACHMENT B